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DEFENSE ISSUES

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As it tries to improve its highly visible acquisition procedures and modernization plans, the DoD acquisition chief discusses these efforts and addresses the recent "revelations" of overpriced spare parts.

Volume 13 Number 26

Acquisition Reforms Save Money and Improve Service

Prepared statement of Jacques S. Gansler, undersecretary of defense for acquisition and technology, to the Acquisition and Technology Subcommittee, Senate Armed Services Committee, March 18, 1998.

Mr. Chairman, Sen. [Joseph I.] Lieberman, members of the subcommittee and staff.

I appreciate the opportunity to appear before the subcommittee ... today to report on our acquisition reform efforts. I am pleased to have with me the senior acquisition executives of each of the services and Brig. Gen. Tim Malishenko, commander, Defense Contract Management Command. Before taking your questions, I want to spend a few minutes summarizing our current defense acquisition posture and my priorities for achieving our overall transformation goals. Following my presentation, all of us will be pleased to answer any questions you have.

When I appeared before this subcommittee last week, Mr. Chairman, to report to you on our overall acquisition strategy, I spoke of a common vision that all of us sitting in this room share: a 21st century combat force that is fast, lean and mobile, prepared for battle with total battlespace situation awareness, able to strike with precision under all conditions and protected with full information assurance. This is the goal of the "Revolution in Military Affairs."

We also share a vision about the way that combat force will be sustained. The 21st century warfighter will be supported by a logistics team that is fully adaptive to the needs of dispersed and highly mobile combat teams -- combining advanced, secure information technology and modern transportation systems to deliver rapid crisis response, track shipments en route, redeploy them if necessary and provide sustainment directly at all levels of operations -- a rapid and smooth flow from factory to foxhole.

Our vision for the acquisition work force that supports our combat forces is a team of highly professional men and women who focus on managing suppliers, rather than supplies -- professionals who perform those functions that fulfill the core responsibility of the department: policy management, budgeting and oversight.

For our vision to become a reality, the Department of Defense must undertake a revolution in the way that we do business. Although our military is clearly the strongest in the world, our defense establishment is still working to keep pace with a commercial sector that, restructured, re-engineered and revitalized, is now thriving in a dynamic global marketplace. We must capitalize on the lessons we have learned from successful commercial restructuring to adopt modern business practices, consolidate and streamline, embrace competitive market strategies, and eliminate or reduce excess support structures.

Acquisition reform, Mr. Chairman, is not a slogan. It is a fundamental transformation in our organization, structure, policies and processes -- one which our acquisition work force welcomes and which we all will work hard to achieve. It is an undertaking that the Congress has supported in the Defense Acquisition Workforce Improvement Act, the Federal Acquisition Streamlining Act, the Federal Acquisition Reform Act and the Information Technology Reform Act -- major legislative initiatives which put the full authority of Congress and the administration behind this effort. Its goals are clear: to do the job better, faster and cheaper. We are transforming the way we do business -- cutting

costs and infrastructure -- to free up funds for modernization.

Today, we will report to you on the progress we have made and our plans for the future of acquisition reform.

During the past few years, we have undertaken some significant efforts and have made measurable gains, but we still have a long way to go. A cultural change of this magnitude takes time -- and sustained effort. For the last 10 years, we have put off modernizing our forces, with procurement spending dropping by more than 70 percent. We can no longer put off modernization. We must maintain our superior level of combat readiness and force structure and improve our equipment quality and responsiveness -- and do all this at lower cost.

This can and will be done. To prove it can be done, I point to what U.S. world-class commercial companies have demonstrated over the past few years in order to become competitive. They focused on time as the critical variable. They have shown that they can develop and deploy with a much-reduced cycle time, meet faster support response time requirements for parts delivery, deal with unanticipated surge requirements, and overall, perform at much higher levels. All this reduces costs. Let me give you just two examples of the potential for dramatic improvements.

The Department of Defense averages 13 to 15 years from weapon initiation through development to initial production. As budgets have been cut, these cycle times have often been stretched even farther. This is expensive and, worse still, prevents us from deploying modern systems into the field quickly enough.

Boeing Aircraft's rapid development and deployment of the 777 commercial aircraft show us that we can do better. From the time development started until the time the first plane certified for flight rolled off the assembly line was only five years. While this commercial aircraft is in no way as complex as many of the military systems under development, we can still learn important lessons in reducing cycle time from the innovative processes of commercial firms. Long cycle times decrease our flexibility and promote obsolescence. The F-22 fighter, for example, is not yet into production but, with electronic products becoming obsolete in as little as 18 months, already contains outdated parts.

Response time is another serious problem we face. The Army stocks numerous parts manufactured by Caterpillar. Average delivery time for those parts, when a base runs out, range from 21 to 36 days here in the United States or 50 to 68 days overseas. Caterpillar itself resupplies domestic commercial dealers in one or two days and overseas dealers (in 100 countries) in two to four days at most -- or they pay for it. To achieve these results, they use modern information technology and rapid transportation, instead of carrying huge inventories. And our volume is not an acceptable excuse: During the height of Operation Desert Storm, military requisitions peaked at 35,000 deliveries per day (on a three-day moving average) -- far short of the performance of commercial package systems (such as FEDEX and UPS) that handle millions of packages overnight.

Our acquisition programs are a legacy from a relatively stable era of known threats. The enemy's moves were fairly predictable, and long-range programs could be structured to meet the limited range of hostile activity we faced. This is obviously not the case today, and our acquisition models for the future must take this into account.

We live in an uncertain and unpredictable world, a world where individual terrorists, transnational actors and rogue nations can unleash firepower in many ways as terrifying as that of a major global power. They represent a different and difficult challenge to forces organized and equipped around traditional missions. They are willing to employ weapons of mass destruction (chemical, biological and nuclear). Also, they have access to much of the most advanced technology and skills through the worldwide arms market. Finally, they cannot easily be deterred, and they often respect no boundaries, whether political, organizational, legal or moral.

This threat militates that we put in place an acquisition system that can field products and systems quickly -- within greatly reduced cycle time. Providing our 21st century warfighter with systems and

sustainment on an accelerated timetable should dramatically improve readiness -- and save money. We are changing to meet the requirement of greatly reduced cycle time and we will accelerate that transformation as our acquisition reform initiatives continue to gain momentum.

Therefore, as I look to the future, I see three main tasks ahead of us: to modernize our current weapons systems, to develop and deploy the major new systems and subsystems required for 21st century operations, [and] to support those systems efficiently and effectively -- and do all three of these at lower cost within drastically reduced cycle times and with greater performance. Last week, in my testimony before this subcommittee, I outlined the steps we will take to complete these tasks and fulfill our modernization goals -- essentially addressing the issue of "what we buy." Today, I will report to you on the other side of the coin -- how we buy it and how we sustain it.

Last week, we discussed the likelihood that, although there will be no major increase in the total defense budget during the next few years, we must meet our commitment to allocate steadily increased funding to the procurement account to pay for modernization. Therefore, the only way to generate the necessary dollars -- without impacting our warfighting capability -- is to shift large shares of our resources from the support and infrastructure area (which now takes more than 65 percent of our total dollars and occupies over 60 percent of the people employed by the department) into the combat and modernization area and to do this while achieving better quality and improved readiness.

This will require a fundamental transformation in our acquisition and support programs. We must pay for our Revolution in Military Affairs by engaging in a Revolution in Business Affairs. To do this, I have set in motion five priorities for our acquisition team:

- Continued Acquisition Reform

We will aggressively pursue and fully implement the acquisition reform initiatives of the past few years; and add to these where appropriate. As the members of this subcommittee know well, real reform in our acquisition of weapons and major systems has taken place in recent years -- reform made possible by your leadership and commitment and by a partnership for reform that includes the Congress, the department and the industrial sector.

This reform must continue to spread to all other areas and become part of the way every one does business -- e.g. better inventory management, an increase in the use of commercial practices and distribution systems to satisfy materiel requirements, more competitive sourcing of current in-house work and greatly expanded purchase of common-use, commercially-available items.

- Civilian/Military Industrial Integration

We must work to bring about far greater civilian/military industrial integration. We seek a greatly expanded partnership with a revived and prospering commercial industry -- not a partnership in which we become simply the pawns of commercial products and processes, but a dynamic and vigorous engagement that, through research and development, creates technically advanced products and systems with common applications and that, through use of flexible manufacturing, allows production of defense-unique items on the same lines with high-volume commercial items.

One example of the latter, that comes to mind, is TRW's production of military-unique circuit boards for the Air Force's F-22 fighter aircraft and the Army's Comanche helicopter on the same production line as its high-volume commercial electronics products. This has resulted in 30 [percent to] 50 percent savings and a product that actually exceeds our requirement for operating in a high-temperature environment.

Modern, "flexible" manufacturing of differing products on a common production line will allow this concept to greatly expand in the future. To achieve this we must reduce or eliminate, where practical, those unique terms and conditions (including unique cost-accounting systems) we previously established for doing business with the government. This will not only improve the department's ability to get goods and services faster, better and cheaper, but will also help our domestic industrial market compete in the global arena.

Let me give you just two examples of how shifting to commercial practices saves us money. The Defense Logistics Agency has used commercial buying practices and purchased high-quality commercial items (instead of military-standard items) which, from a sample of more than \$190 million worth of items, resulted in savings of more than 20 percent in medical supplies and 22 percent in clothing and textiles. The logistics response time differential, due to using commercial practices, improved by 50 percent and, when prime vendor practices were used, improved by 95 percent.

Using commercial business practices over the past five years, the DLA wholesale inventory alone was reduced \$721 million, a 30 percent savings. This shows the dramatic savings that can result when we adapt commercial practices to our military requirements. These practices must become widespread!

As you know, Mr. Chairman, there have been isolated instances where we have failed to carry out properly the changes we are making. I am certain that you appreciate the fact that, as we begin what amounts to a complete restructuring of the way we do business, we are going to make a few mistakes. That is regrettable.

Such an error was made, for example, in dealing with two commercial suppliers. In the first case, we paid more for sole source commercial items purchased from the company's catalog than we had paid for the same items when we obtained cost data from the company (something the buyer should have observed, but failed to do). We also made repetitive purchases without leveraging our buying power to get substantial discounts off the catalog price. When this was found, we worked with the department's inspector general to investigate the problem and came up with solutions.

We are now providing additional guidance and training to our acquisition work force on obtaining fair and reasonable prices for commercial items. We have negotiated a single contract for these parts, based on all the department's requirements, and were able to obtain a substantial discount off the company's catalog prices.

In the second case, we negotiated a contract for direct delivery on an "as needed" basis. This contract eliminated the need for us to forecast, warehouse and maintain these parts. The company guaranteed delivery of these parts at specified locations within agreed-upon time frames. We then mistakenly issued orders against the contract for large quantities of parts for delivery to our warehouses.

The price we paid was too high because the contract was based on delivery of small quantities for direct delivery to specific locations. Some of these parts were also mistakenly coded as "sole source" when they should have been purchased competitively. As a result, the Defense Logistics Agency has been working with its hardware centers to ensure that this contract is used as intended, that specific actions are taken to improve corporate contracts overall, that additional training is made available, and that detailed policy guidance on determining fair and reasonable prices for commercial items is provided to contracting offices. These improvements will help us to correct problems we have identified.

The mistakes we made in these isolated cases were based upon a number of factors. We failed to take advantage of our buying power and we failed to understand what we were buying and what was included in the prices. We responded quickly to these mistakes. We developed training to help our buyers better understand the new dynamic our changed marketplace provides and we are developing tools to help them make better decisions.

What is important to emphasize is that these were isolated and rare cases. In the overwhelming majority of cases, using commercial practices and buying commercial items has paid huge dividends in savings, responsiveness and quality.

- Support and Infrastructure Restructuring

The department must take specific actions to shift the major share of its resources from support to modernization and combat. Reducing support and infrastructure costs will make more of our limited funds available for modernization and deployment of new systems and subsystems. Another critical

element is competitive sourcing of all noninherently governmental work.

For example, DoD has routinely used public/private competitions (under the provisions of OMB Circular A-76) that have resulted in about a 50-50 split on public/private winners and a 20 percent average savings when the public sector won and close to 40 percent savings when the private sector won -- thus demonstrating that we can and do benefit significantly when we introduce competition into the commercial activities arena.

With further rounds of BRACs [base realignment and closure] in 2001 and 2005, (which are an essential part of our overall transformation strategy), greatly expanded competitive sourcing and other such actions to achieve infrastructure and support reductions, we can shift tens of billions of dollars a year to modernization and combat -- while actually improving our support to the forces!

- Re-engineer DoD Logistics

We must totally re-engineer our DoD logistics system. The goal of "focused logistics," outlined by the Joint Chiefs of Staff in [Joint] Vision 2010, which will ensure that our combat forces have the right equipment on hand at the right time, is a high priority for all of us as we support the Revolution in Military Affairs. Advanced information systems and rapid transportation are keys to our success in this area. I can assure you that this is an area that we are pursuing aggressively and immediately.

- Work Force Enhancement

Finally, we must focus on training and educating our acquisition work force to meet the demands of this massive transformation effort. Training our work force in new ways of doing business must be our No. 1 priority. Unless we all know how best to do what we are doing and comprehend the benefits to be derived from doing it better, acquisition reform will not succeed.

A solid foundation for the education of the work force has been established under the Defense Acquisition Workforce Improvement Act. Today, Defense Acquisition University courses are moving from the traditional classroom to sites where the work force is located. A modern "distance" learning plan will evaluate, by FY [fiscal year] 2000, all acquisition courses taught by the Defense Acquisition [University] and convert as many as feasible and desirable to distance learning and computer-based training. Our goal is to convert at least 25 percent of the Defense Acquisition University courses to distance learning by the end of FY 99.

Since 1989, the department has reduced the work force in acquisition organizations by more than 42 percent -- over one-quarter [of a] million people. We have learned to operate effectively and efficiently with such reductions. However, we also know that infrastructure must continue to shrink if we are to continue to afford modernization and readiness.

Congress has ordered the department to reduce the work force in acquisition organizations by the beginning of next fiscal year. The undersecretary of defense for personnel and readiness is working with me to determine the maximum possible reduction we can make without sacrificing military readiness and the efficient management of the acquisition system. A report is due June 1 of this year.

Also, Section 912 of the National Defense Authorization Act for Fiscal Year 1998 requires the department to review the acquisition community to develop a plan to streamline the work force, organizations and infrastructure. This is an opportunity to examine the current structure in light of advances in commercial practices, processes and information technology. Our report to the Congress on Acquisition Workforce Reform is due on April 1.

As you can imagine, Mr. Chairman, there are significant barriers to implementation of the reforms I have discussed today. Therefore, one of the major requirements of our transformation strategy is the development of a specific action plan for meeting our goals. We have set hard targets and tough standards to measure the progress of our reform efforts. We have established interim milestones and a layered set of metrics to determine how actual accomplishments measure up to Secretary Cohen's

Defense Reform Initiative and to the quantitative goals we have committed to the vice president in the National Performance Review -- in areas such as development cycle time, support response time, weapon system cost reduction and paperless business processes.

We also need the continued commitment and support of Congress -- as you have provided in the past. Acquisition reform will provide the resources to do that. I appreciate your past support and count on your continued support to meet these goals.

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